Service Date: February 9, 1981

DEPARTMENT OF PUBLIC SERVICE REGULATION
BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MONTANA

* * * * *

In the Matter of the Application of	)	UTILITY DIVISION
The MONTANA POWER COMPANY for	)	DOCKET NO. 80.4.2
authority to Establish Increased Rates	)	ORDER NO. 4714b
for Electric and Natural Gas Service.	)	

FINDINGS OF FACT
MPC Motion

1. On April 8, 1980, Montana Power Company (MPC, Applicant) filed an application with the Montana Public Service Commission for an order authorizing the Applicant to increase rates for electric and natural gas service to defray increased costs of operation and maintenance.

2. On December 19, 1980, Order No. 4714a was issued Docket No. 80.4.2. This order granted the Applicant an increase in electric and natural gas rates rendered on and after December 19, 1980.

3. On January 12, 1981, the Applicant filed a request for reconsideration of Order No. 4714a requesting the Commission to authorize an increase in rates based upon six arguments.

4. On January 12; 1981 the Great Falls Gas Company, an intervenor in Docket No. 80.4.2, filed a Motion for Reconsideration of Commission Order No. 4714a. The motion asked for reconsideration on the grounds that the volumetric allocation method adopted by the Commission in Order No. 4714a resulted in a "price squeeze" that provided the Montana Power Company, a competitor with Great Falls Gas Company, with an unfair competitive advantage .

5. On January 26, order denying the Motions to Reconsider submitted by the Montana Power Company and the Great Falls Gas Company. 1981 the Commission directed its staff to draft an

PART I

THE MONTANA POWER'S MOTION FOR RECONSIDERATION

Coal Expenses

6. The Montana Power Company raises the following points in challenging the Commission's determination regarding its treatment of coal expenses for rate making purposes:

The Commission ignored the testimony of John O'Leary on the issue:

The Commission's decision was not 'based ' on reliable evidence:

The Commission applied a more 'stringent ' standard for the Company's; evidence on the issue than it did to the Montana Consumer Counsel's presentation:

The Commission improperly ''determined the proper 'transfer price for coal:

The Commission's order unlawfully regulates Western Energy, a company not subject to the Commission's jurisdiction.

7. The Commission found that the Montana Power Company failed to establish the reasonableness of the price it pays to its wholly owned subsidiary, Western Energy, for coal used in the Corette and Colstrip plants. The Commission continues to believe that price is the only issue before it in this docket. Because that issue was not addressed by John L. O'Leary, witness for MPC's common shareholders, it was not necessary to discuss his testimony in Order No. 4714a. By his own admission, O'Leary did not appear before the Commission as an expert in coal pricing, and made no independent analysis of the arrangement between

Western Energy and the Company. (Tr. 635) Further, O'Leary's testimony seems to assume that adoption of MCC witness Wilson's recommendation is tantamount to the Commission extending its regulatory jurisdiction to Western Energy's operation. As discussed in the order, and subsequently in this order, the Commission rejects this assumption and testimony upon which it is based.

8. The Company's motion attacks the reliability of Wilson's testimony, claiming that it is less reliable than that presented by the Company. This self-serving statement cannot seriously be considered. The Company, in its rebuttal of Wilson's testimony, offered no evidence that Wilson's "comparable coal industry earnings" exhibit was faulty, and itself used portions of the Justice Report which it now criticizes Wilson for using. It should also be noted that the Company did not object to the portion of Wilson's testimony which includes citation to this report. The record reveals no impeachment of Wilson's testimony and the Company offers nothing in the way of impeachment in its Motion. The Company's criticism amounts to nothing more than a disagreement with the way in which the Commission weighed the evidence presented .

9. Similarly, the Company argues that the Commission applied a more stringent standard to the Company's evidence than it did to the Consumer Counsel's evidence. With this the Commission does not agree. The Order demonstrates that the Commission merely analyzed the parties' testimony and found the Company's assertions adequately rebutted by the Consumer Counsel's testimony. Had the Company wished to challenge Wilson's testimony, it had ample opportunity to do so on rebuttal and through cross examination. The Company cannot do in a Motion for Reconsideration what it chose not to do during the. proceedings which developed the record upon which the commission based its decision.

10. The Company's arguments that the Commission improperly determined the transfer price for coal and that it is, by its order, regulating Western Energy are simply two parts of the same issue, i.e., what methods are available to the Commission to assure ratepayers that excessive prices are not being paid by a regulated utility to its wholly owned coal subsidiary.

The Commission was presented with three methods in this docket, the comparable price method, the comparable profits method and the rate of return method. For reasons outlined in the Order, the Commission relied primarily on the rate of return method and secondarily on the comparable profits method. Under any of these methods, the price paid by the Company to Western Energy might be reduced. Each method merely offers the Commission guidelines by which to judge whether a regulated utility is paying too much for coal bought from its subsidiary. The Company fails to make any showing demonstrating why a potential decrease in allowable expenses under the comparable price theory does not constitute regulation of Western Energy while the same decrease under the rate of return theory does constitute such regulation. The Commission finds no logical or legal basis for such a distinction.

11. The Commission finds no basis upon which it should at this time receive the Arthur D. Little study into evidence. In denying this portion of the Company's Motion for Reconsideration, the Commission adopts the cogent reasoning contained in Suggestions of Montana Consumer Counsel In Opposition to Motion for Reconsideration of Commission Order 4714 of The Montana Power Company. It should be further noted that the report was first made available to parties October 7, 1980 (the first day of the hearing), although the Arthur D. Little Company had reported their results to MPC by the time the rate case was filed, April 8, 1980. The Company made no attempt to explain why its consultant was unable to make the report available in a timely fashion.

12. The Company is well aware that the Commission's practices and procedures contemplate prefiling of testimony and exhibits according to a procedural order, the establishment of which is done in consultation with all interested persons. Ail parties rely on this procedure in' preparing their cases. This procedure is especially important for intervenors who must rely on out-of-state expert witnesses, whose schedules are often quite inflexible.

13. Had the Commission allowed the Little Report into evidence, intervenors would have had no opportunity to review it or to adequately prepare cross-

examination and answer testimony. A fair airing of the technical issues contained in the Report would' have been impossible.

14. As the Company is well aware, the Commission has been flexible in allowing-additional testimony not contemplated by its procedures when to do so would not unfairly prejudice the interests of other parties. Such flexibility was demonstrated in this case when the Company was allowed to submit Supplemental Testimony which reflected an unexpected reduction in gas sales. In this and future cases, the Commission will reject untimely submissions of testimony when to do otherwise violates basic tenets of fair notice.

Investment Tax Credits

15. In argument No. 4 of its Motion for Reconsideration, the Applicant points out that post-1970 Investment Tax Credits are included in the rate base. In Finding of Fact No. 17 the Commission stated that deferred taxes are excluded from rate base. The order should state that pre-1971 Investment Tax Credits are excluded from rate base.

16. The amounts attributable to pre-1971 Investment Tax Credits are removed from rate base. The Commission removed Investment Tax Credits from the capital structure to achieve consistency with the rate base treatment noted for pre-1971 items. The real issue is whether or not Investment Tax Credits should be part of the Applicant's capitalization. For the purposes of this proceeding the Commission finds the exclusion of Investment Tax Credits from the capital structure proper.

17. Applicant's argument No. 5 in the Motion for Reconsideration asks that the Commission reserve acceptance of the amortization of the excess balance due to a change in income tax rates pending the issuance of regulations by the IRS. The Applicant goes on to note the caution the Commission exercised in adopting full normalization and seeks to cover both issues with the same blanket, urging similar caution in treatment of the excess balance.

18. The change, in the corporate tax rate from 48 percent to 46 percent is a known and measurable change. To allow an incorrect accrual for future tax expense would be patently unfair to ratepayers. The testimony regarding risk of loss of the accelerated depreciation option due to this adjustment was not persuasive in the view of the Commission.

Gas Supply

19. The Commission is aware that MPC's Motion for Reconsideration does not seek a change in Commission Order No. 4714a but rather ' "states the Company's position with respect to the Commission's disposition of certain issues related to natural gas utility operations....." The following findings are offered for clarification as the Commission's position was stated in Order No 4714a.

20 . The Company identifies several areas of concern to it regarding the natural gas utility:

A. The exploration and development (E&D) program authorized by the order is not instantly achievable

B. The Commission should maintain an awareness of capitalized versus expensed amounts in achieving the E&D program contemplated by the order.

C. The Commission has impinged on management discretion in adjusting the gas mix structure.

21. In response to the first concern, the Commission Staff requested that MPC provide a target date for achieving the $10 million annual expense level provided for in the order (response attached as Appendix A). It was

stated in the response that a good faith effort would be exerted to achieve the ordered expense level "in the last quarter of this year or the first quarter of

1982..." Consistency with the order dictates that the $10 million expense level to be achieved within one year of the order date be an accumulation of 12 preceding months expenses rather than achievement of an expenditure level that would on a pro forma basis produce a $10 million expense level.

22. The Company's second area of concern can be alleviated by a view of the schedule on page 48, Order No. 4714a. It is evident that $10 million has been provided for the expense portion of the Company's E&D program. Under the successful efforts method of accounting described by company witnesses, expenses associated with wells capable of production are capitalized while those associated with "dry holes" are expensed. A larger than $10 million E&D program is therefore implied, given the history of company E&D where some amounts have been capitalized and some expensed.

23. The Commission finds that its position is sufficiently expressed in Order No. 4714a regarding the Company's final contention.

24. In light-of the Company's confusion pertaining to E&D findings in Order No. 4714a, the Commission contemplates investigating a procedure which would reduce the balance in the Company's deferred gas cost account by the difference between the $10 million Montana E&D expense amount allowed in the order less the amount actually expensed for Montana E&D, if materially lower.

Additional Testimony

25 Mention must be made of the Company's attempt, via its Motion for Reconsideration, to introduce facts not in evidence Those "facts" are competently summarized in the Consumer Counsels Comments on the Motion. Such attempts must be condemned by this Commission as being a brazen effort to circumvent the legal requirements for evidence which may be properly considered by the Commission in reaching its decisions.

PART II

THE GREAT FALLS GAS COMPANY'S MOTION FOR RECONSIDERATION

1. Findings of Fact Nos. 134 through 171 in Order No. 4714a set forth the philosophy underlying the volumetric allocation of costs technique first adopted by this Commission in Order No. 4521b, and discusses at great length the issue of discriminatory rates to the Great Falls Gas Co.

2. Much of the basis for Great Falls Gas Company's Motion for Reconsideration lies in their argument that the wholesale price of gas from Montana Power to Great Falls Gas is approximately 21/2 cents per Mcf lower than the rate charged by Montana Power to its retail customers. In making this comparison, however, the Great Falls Gas Co. has once again failed to take into account the pressure differential at which these two volumes are sold. The Great Falls Gas Co. purchases gas from the Montana Power Co. at an average pressure base of 14.9 psia. The Montana Power Co. retail sales are sold at an average pressure base of 12.95 psia. When wholesale and retail sales are put on an equivalent pressure basis of 14. 9 psia the wholesale rate to Great Falls Gas is approximately 37 1/2 cents per Mcf lower than the retail rate to Montana Power Company's residential customers, not 2 1/2 cents per Mcf lower as claimed by Great Falls Gas.

3. The Commission strongly disapproves of the Great Falls Gas Company's consistent inaccurate characterization in comparing its gas prices to those charged to MPC's residential customers. By so doing, it has caused widespread misunderstanding and confusion among its customers. As the Company is very well aware, a comparison of prices for gas at different pressure bases is meaningless. Should the Company choose to continue its apparent policy of misrepresenting the price disparity between MPC's utility and residential customers in papers filed with this Commission in the future such papers will be returned for correction. The merits of any position taken by the Company in its filings will not be considered by the Commission until such corrections are made.

4. The issues as raised by Great Falls Gas in their Motion for Reconsideration are not substantially different from the issues raised by Great Falls Gas regarding

discrimination in the Montana Power general rate case in which the Commission found:

a) that, the volumetric allocation methodology is ,the most appropriate method of allocating costs given today's market conditions and the fact that the commodity has become a much more relatively scarce good than the facilities used to transport the commodity,

b) that none of the customer or distribution costs associated with the Montana Power Co. system were allocated in any way to the customers of the Great Falls Gas system,

c) that the volumetric allocation technique allocates costs on an even-handed basis to all of the customers of the Montana Power Co. and, hence,

d) there is no basis for the allegations of discrimination as put forth by the Great Falls Gas Co.

5. The Commission finds no reason to believe the facts and conclusions found in Order No. 4714a are less compelling today than they were at the time the Order was issued.

Price Squeeze

6. The allegations of "price squeeze" as presented by the Great Falls Gas Co. are based on the "zone of reasonableness concept as outlined in Federal Power Commission v. Conway Corp., 426 U. S. 271 (1976). Great Falls Gas argues that the finding in that case was that although divergent retail and wholesale prices may both fall within the zone of reasonableness, the disparity may be so insignificant as to warrant a claim of price squeeze in that the small differential provides the wholesaler an unfair competitive advantage at the retail level. To this end Great Falls Gas cites from a decision by the Court of Appeals in which it was found that "(t)here would, at the very least, be latitude in the FPC to put wholesale rates in the lower range of the zone of reasonableness, without concern that

overall results would be impaired ".

In considering Great Falls Gas Company's argument me commission would point out that there is no testimony or evidence in either the general rate case or in Great Falls Gas Company's Motion for Reconsideration indicating what the appropriate zone of reasonableness is or should be. Also, the Commission would ask the question. Given an appropriate zone of reasonableness, if 21/2 cents is not a large enough divergence in rates to place the wholesale rate in the lower end of the zone is 37 1\2 cents large enough?

CONCLUSIONS OF LAW

1. The Montana Power Company is a corporation providing electric and natural gas service within the state of Montana and as such is a public utility within the meaning of 69-3-101, MCA.

2. The Montana Public Service Commission properly exercises jurisdiction over MPC's operations pursuant to Title 69, Chapter 3, MCA.

3. The Commission acts in its legislative capacity when it allocates utility costs to the various customer classes.

4. The Commissions adjustments to the Company's gas supply costs and coal costs do not usurp the management prerogatives of the Company.

5. The expense adjustment relating to coal purchases is necessary in order for the Commission to meet its legal obligations as set out in 69-3-201, M CA.

6. The rates approved by Order No. 4714a are just, reasonable and not unjustly discriminatory.

7. The rate base adopted in Order No. 4714a reflects original cost depreciated values and as such complies with the requirements of Section 69-3-109, MCA, that

the value placed upon a utility's property for rate making purposes " . . may not exceed the original cost of the property. "

8. The rate of return allowed meets the constitutional requirement that a public utility's return must be "commensurate with returns on investments in other enterprises having corresponding risks and sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital." Federal Power Commission v. Hope Natural Gas Company, 320 U.S. 591, 603 (1944).

1. Although the rate base treatment for investment tax credits was correct in Order No. 4714a. Finding No. 17 of that order incorrectly described that treatment; therefore, Order No. 4714a, Finding No. 17 is amended to read:.

With regard to unamortized investment tax credits, the Commission for the purpose of this Docket, does not accept their inclusion in the capital structure. Since pre-1971 Investment Tax Credits are not allowed lin rate base it is consistent to exclude such items from this capital structure.
2. The Montana Power Company's Motion for Reconsideration is denied.

3. The Great Falls Gas Company's Motion for Reconsideration is denied.

Dated this 2nd day of February, 1981.

BY ORDER OF THE MONTANA PUBLIC SERVICE COMMISSION.

ATTEST:

Madeline L. Cottrill
Secretary

(SEAL)

GORDON E. BOLLINGER, Chairman

JOHN B. DRISCOLL. Commissioner

HOWARD L. ELLIS, Commissioner

CLYDE J. JARVIS, Commissioner

THOMAS J. SCHNEIDER, Commissioner